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SUBJECT: Minister of Investment Talks Economic Reform, Privatization and Elections

11. (SBU) KEY POINTS

- Investment Minister Mahmoud Mohieddin told the Ambassador that successes in the Egyptian economic reform program have helped mitigate the impact of the global economic crisis.
- The Ministry of Investment looks to the USG for continued support and technical assistance.
- Sustainable growth continues to be an issue for the GOE, and Mohieddin does not expect much near-term progress on economic reform given the current economic and political environment.
- The MOI plans to release a revised version of its privatization scheme soon with more details on broadening ownership, protecting the interests of future generations, and establishing a professional asset management agency to manage the process.

12. (SBU) On July 1, the Ambassador met with Egyptian Minister of Investment Mahmoud Mohieddin to discuss the current state of economic reform and the effect on the bilateral relationship of President Obama's speech. Mohieddin talked about the newly implemented single non-bank financial regulator (EFSA) which had come into existence that day. The EFSA places all non-bank financial institutions under one roof for better coordination of regulation. He said that he was "very pleased" about the single regulator and that the new regulatory structure was not simply a response to the financial crisis, but was the result of a project begun with the 2003 financial sector reforms.

13. (SBU) If the global financial crisis had hit in 2004, he added, "we would have been in trouble" since the economy at that time was marked by weak balance sheets, poor corporate governance, bad loans, and ailing insurance companies. He said that Egypt appreciated the "kind support" of the U.S. in financial sector reform in banking, insurance, and mortgage finance. He said that in the next few years the GOE will decide if banks will continue to be regulated by the central bank or if they will move regulatory supervision to the EFSA.

14. (SBU) The Ambassador told Mohieddin that she was glad to hear that USAID had achieved goals set several years ago and added that the USAID was now developing a new strategic approach. For the U.S. and Egypt, it is time to reframe our objectives, and she added that the next two years will be transitional years as we move to a new approach.

15. (SBU) The Ambassador said that when President Obama talked about expanding cooperation with the Muslim world, he was talking about countries like Egypt. There is a desire to expand programs in education, science and technology, and democracy and governance, she said, adding that the level of U.S. assistance was unlikely to rise and the days of large cash transfers are over. Mohieddin responded that at this point "technical cooperation is more important than

financial support."

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#### Expanding Access to Financial Services

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¶6. (SBU) The USAID Mission Director raised the issue of broadening access to financial services beyond the privileged top 10% of the population. Mohieddin agreed, saying that there has been a slight improvement but "nothing to be impressed about." He pointed out that the majority of Egyptian companies are small with 90% of corporations having less than LE 10 million (US\$1.8 million) in issued capital, and 70% have less than LE1 million (US\$180,000).

¶7. (SBU) Mohieddin said that access to finance for SME and microfinance continues to be a focus of financial sector reform. In response to a question by the Ambassador, he confirmed that microfinance lenders will continue to be regulated by two separate regulatory frameworks-- the new EFSA will regulate microfinance companies, and the Ministry of Social Solidarity will continue to regulate NGOs that provide microfinance services. He added that regulatory oversight of issues such as terrorist finance and combating money laundering will apply to microfinance NGOs as well.

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#### Economic Reform Slowed by Inflation and Credit Concerns

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¶8. (SBU) Mohieddin said that the pace of economic reform had slowed over the past 18 months as a result of the sharp increase in food and fuel prices in 2008 followed by the onset of the global credit crisis. He added that commodity price inflation had a larger impact

on Egypt than the credit crisis. Since then, external factors have improved, and Egypt expects inflation of less than 10% "for a while," though commodity prices have been creeping up this year.

¶9. (SBU) Mohieddin said that the GOE is trying to continue reforms, but for the time being the focus would be more short term. The Ministry of Finance is concentrating on controlling the budget deficit, and the GOE is challenged by how to maintain high growth. He told the Ambassador that the second quarter growth rate had exceeded lowered expectations, and since 60% of Egypt's GDP comes from domestic demand, Egypt can survive "for a while" by relying on domestic demand. However, he added that while a GDP growth rate of 4.5% is good for this year it is not sufficient in the future. Egypt continues to face problems of poverty, high unemployment, low salaries, and a low standard of living. "6% is the critical minimum" growth rate needed to improve the situation in Egypt, he said.

¶10. (SBU) Mohieddin suggested that the Egyptian economy needed to diversify further and that the GOE could take other measures to stimulate growth such as cutting interest rates and making more aggressive infrastructure investments. He said that a plan covering 52 new infrastructure projects has been presented to President Mubarak, but "this government will not do anything dramatic." When asked, he told the Ambassador that subsidy reform was unlikely this year, but that the issue of energy subsidies will be revisited in 2010, and that January could see the announcement of an "interesting approach" to subsidies. Lower oil prices have eased some of the financial burden of subsidies and the GOE's fiscal budget assumptions for the price of oil have been reduced from \$120 to \$60-70 per barrel. Energy, he pointed out, represents 75% of the GOE subsidy bill and amounts to five and a half times education spending and six times the level of health spending.

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#### Privatization: Next Steps

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¶11. (SBU) Mohieddin said that the GOE privatization initiative would continue and that there would be an announcement in two weeks regarding the next steps on privatization. He said that the key pillars of the program would be broadening ownership, protecting the interests of future generations, and establishing a professional asset management agency to manage the process. He said that the

initiative would now cover 86 companies (twice as many as originally proposed) but will not include everything from the original proposal. The distribution of free shares would not be conducted, and shares would be sold only to Egyptians. The new proposal would include the establishment of a "future generations fund" into which some of the privatization proceeds would be deposited. Though the plan is not perfect, he said it covers "80% of what I wanted."

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Elections  
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¶12. (SBU) Mohieddin told the Ambassador that the current Nazif government is "cruising" and is not pursuing any aggressive reforms. He said that after 2010 elections, a new government may take "bold steps". When asked by the Ambassador if he expected early elections (of the People's Assembly) to be called this summer, he replied that "I have no information, but it could happen."

¶13. (SBU) He added that there is no dispute between the government and parliament, which is the normal cause for early elections, but that there are a number of issues that would be resolved if early elections were held including several disputed seats as well as the 64 new Assembly seats dedicated to women legislators. "We've been asked by the Secretary General of the NDP to be ready," he added. The Minister said that the mere talk of early elections has motivated parliamentarians to work harder for their constituents. He said he "would like to see elections sooner to encourage the government to take action sooner rather than keeping the wait and see attitude."

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Obama Speech Follow-up  
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¶14. (SBU) With respect to President Obama's speech, Mohieddin said that the President covered many issues that are important to the agenda of his ministry. He said that Egypt would be happy to participate in a follow-up summit. He hoped that the speech would encourage entrepreneurship and a larger role for "new blood" such as the Egyptian Junior Business Association. The Ambassador told Mohieddin that one of her goals was to help raise the education level of young Egyptians to a global level. She discussed her ideas

of working with model schools and both the public and private sectors to enhance the level of science education. Mohieddin said that human capital investment through education was critical and talked about new British university scholarships that the Ministry had established.

¶15. (SBU) During the meeting, the Minister told the Ambassador that he planned to travel to the U.S. in September as part of an "investment roadshow" being put together by the American Chamber of Commerce in Egypt (AMCHAM).

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